

Regulation of International Financial Center: A Comparative Study of Financial Consumer Protection in China and U.S.

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Abstract

The U.S. financial consumer protection system is well known for its comprehensiveness. But after the eruption of the sub-prime mortgage crisis, the U.S. government realized the lack of consumer protection is the major cause of the financial crisis. As to China, it is urgent to establish a sound financial consumer protection system. We should do more research on China's financial consumer protection system, find out problems and resolve them and learn from the advanced country, such as the U.S.

Keywords

International Financial Center; Financial Consumer Protection; Financial Legislation

Introduction

In 2009, both the State Council issued Opinions on Promoting Shanghai to Speed Up the Development of Modern Service Industry and Advanced Manufacturing, Building an International Financial Center and the Views of an International Shipping Center and the Standing Committee of Shanghai Municipal People's Congress approved Regulations of Shanghai Municipality on Promoting the Construction of the International Financial Center, marking the new historical stage of the construction of Shanghai International Financial Center.

In China, financial legislation is financial regulatory legislation according to the characteristics of financial markets.

Chinese current financial regulation can be divided into three sectors as banking, insurance and securities based on its market functions. While based on two main targets of financial regulation, it can be divided into two sectors as the protection of consumer rights and the stability of financial system.

China's running financial legislation is more prior to the stability of financial system but less protection to the financial consumer rights. Public laws' target of interest balance requires balancing different interest among different main body. Nevertheless, the extreme imbalance of interest will break through the institutional framework and damage public interest.

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The issuance of Blueprint for a Modernized Financial Regulatory Structure in 2008, the announcement of Consumer Financial Protection Agency Act of 2009 and the approval of Dodd-Frank Wall Street Reform and Consumer Protection in 2010 clearly enhanced the regulatory authorities' responsibilities and measures on consumer protection.

It has become the major content of reflection and reform for many countries to strengthen financial consumer right protection after the financial crisis. As the emerging country or regions, Shanghai could learn from US's financial legislation, especially to the aspect of financial consumer protection law for building itself as the international financial center.

The Necessity of the Establishment of a Sound Financial Consumer Protection System

There are three fundamental subjects in the legal relationship of finance: Government, operators and consumers. Operators and consumers are the major market players, are not only regulation objects but service objects. Operators are set in a strong position,

which means consumers need more government's protection. The analysis of the necessity of the establishment of a sound financial consumer protection system and be following two aspects:

Objective Reasons

▪ The Negative Externality of Financial Operation Behavior

Financial operations are prone to pursue profit maximization by providing more financial products under limited rationales. The sum of individual institution inadequate rational behaviors can lead to negative externality and make malfunction of financial market or even the whole economic system crisis, for example, the US subprime mortgage crisis. Thus, government should take necessary intervention to financial operators' uncertain and high risk activities in order to increase financial consumers' confidence and protect their rights.

▪ Asymmetric Information Between Financial Operators and Financial Consumers

The complexity and professionalism of financial products lead to asymmetric information. Financial consumers mainly rely on the understanding and accurate valuation of information when receive financial services and purchase financial products. If rights to know are breached, people will suffer more loss. Financial consumer protection can be made by institutionalized education and information disclosure, etc.

▪ Power Disparities Between Financial Operators and Financial Consumer

Financial consumers are set in a weak position for its lack of special knowledge, capital size and the capacity to pursue legal remedy. Moreover, such problem cannot be resolved by market function itself. The fundamental approach is State organs involved by laws and giving consumer special protection to realize the substantive equity between the parties to the transaction.

Significance of Value

To establish a sound financial consumer protection system is:

1. To protect financial consumer interest and improve financial consumption level;

2. To enhance the competitiveness of financial industry and protect interests of financial operators;
3. To promote the healthy development of financial markets and maximize public interest;

Consumer Protection System of China's Financial Status and Problems

Since the beginning of last 90s, China issued series of rules, regulations and other administrative standard documents including *Law of the People's Bank of China*, *Law of Commercial Banks*, *Securities Law*, *Insurance Law*, *Law of the People's Republic of China on Banking Regulation and Supervision*, which systematically constitute the fundamental legal system for banking, securities, insurances, futures and other financial industries or other words, segregated financial system. From the perspective of financial consumer protection, current China financial consumer protection situation and problems can be summarized as follows:

Government's Vagueness on Financial Consumer Protection

Financial legislation is more focus on the safety and effectiveness of financial institutions, ignores the interests of consumers and weakness of the financial safety in financial consumer protection. Chinese current laws in the consumer protection goals are not clear, despite several normative documents issued by the China Banking Regulatory Commission.

Incomplete Financial Legislation on Consumer Protection and Financial Consumer Rights

China's financial consumer protection laws can be divided into three levels: the first is Law of the People's Republic of China on the Protection of Consumers' Rights and Interests, but most rules about consumers' rights and operators' responsibilities are not applicable to finance consumption. The second is Law of Commercial Banks and Law of the People's Republic of China on Banking Regulation and Supervision, which focus on financial regulation, deposit security and confidentiality. The third is departmental rules and regulations issued by the People's Bank of China and the China Banking Regulatory Commission, which mainly formulated restrictive clause and lack of specific operational methods.

Not Bear a Clear Responsibility to Protect Financial Consumers By Regulatory Authorities

Under China's current regulation system, no individual regulatory institution takes the legal responsibility for financial consumer protection, In addition to political petitions.

Additionally, problems include lack of complaints handling mechanism, inadequate financial consumer rights protection and less financial consuming knowledge propagation by financial regulatory institutions..”

Learning From the U.S. Financial Consumer Protection System

The Protection of Consumers' Rights and Interests

It is one of the two basic goals of the U.S. financial legal system to protecting consumers' rights and interests. According to the above mentioned U.S. financial laws, the main content of the American Financial Consumer Protection Law are consumers' rights to know, the protection of consumers' privacy, obligations, safety and fair dealing. After the subprime crisis in 2008, the Obama administration realized that the majority of consumers are in lack of professional financial knowledge, thus facing difficulty in identifying underlying traps behind the financial products. Therefore, it's necessary for those consumer rights and interests protection agencies to strengthen their responsibility for educating consumers.

Protection Agencies

The U.S. federal regulatory system for the protection of financial consumers is consisted of Federal Reserve, Office of the Comptroller of the Currency, the Federal Deposit Insurance Corporation, Office of Thrift Supervision and so on. Protection of consumers is one of their core tasks, complementing to other tasks (such as financial Security and prudential supervision). Now these financial protection agencies established in accordance with the Dodd-Frank Wall Street and Consumer Protection Act are on a mission of supervising all kinds of financial products such as mortgage loans of house and car; credit card; check and savings accounts, etc. The duty for protecting financial consumer is now transferred to these agencies.

The Mechanism for Disputes Settling

In the U.S., banks deal with the consumers' complaints

by themselves, only those cases that they can't deal with will be submitted to those regulatory bodies such as Federal Reserve Board, Office of the Comptroller of the Currency or the Federal Deposit Insurance Corporation etc. First of all, the Federal Reserve Board is in charge of supervising banks and dealing with the complaints against them. Secondly, consumer-supporting department set under the Office of the Comptroller of the Currency is designed to handle complaints against banks. Thirdly, established under the Federal Deposit Insurance Corporation, the "Consumers Response Center" is responsible for handling bank complaints from consumers. If the consumers' rights can't be protected through above agencies, it has to be resolved through the judicial way. Consumers' small claims and class actions, the most common judicial ways, will be applied.

Suggestions for the Legislation of Shanghai Financial Consumer Protection Law

The Definition of Financial Consumers

The definition of financial consumers is the primary legal concept in financial consumer protection system. It can be defined as: subjects who buy and use financial products or receive financial service. The subjects not only refer to consumer as natural person but also include legal person as representative of a company. Usually, they don't work for professional financial agencies and are not equipped with professional financial knowledge, thus are in a disadvantaged situation in the trade.

The Purpose and Principles of Legislation

The legislation of Shanghai Financial Consumer Protection Law is aimed at protecting the lawful rights and interests of consumers, balancing the interests of financial subjects, maintaining the stability of financial order and realizing the maximization of the social and public interests.

From the perspective of concept, it's suggested to clarify the national protection principle, social protection principle, as well as the scientific protection principle (based on financial rules); from the perspective of technology, it's suggested to set up the partial protection principle in terms of attitude, complete protection principle in terms of content and proper protection in terms of execution.

Content of Protection

Under the guideline of the complete protection principle, Shanghai Financial Consumer Protection Law should include protection of traditional and newly-invented financial products that consumers buy and use, as well as old and new financial service that the consumers receive.

Rights and Interests in Protection

The rights and interests of financial consumers can be divided into nine categories:

(1) Safety rights; (2) Rights to know; (3) Freedom of choice; (4) Fair trade Rights; (5) Compensation rights; (6) Rights of association; (7) Education rights; (8) Right to be respected; (9) Supervision rights.

Consumer Protection Agency

The current financial regulatory system in China applies Specialized Supervision. We can refer to a series of protection modes adopted recently by the USA so as to better protect our financial consumers. Considering the important status of Shanghai in China's legislation work, it's recommended that shanghai financial office should take the lead in setting up a coordination and supervision mechanism among agencies. Meanwhile, due to the fact that the power of Shanghai financial regulators is limited and it takes time to get instruction from the decision center, we suggest that the State Council might approve the establishment of Shanghai Financial Regulator Headquarter, or endow shanghai financial regulator with more power in terms of supervision and regulation.

Mechanism for Resolving Disputes

As for the Financial Consumer Dispute Resolution Mechanism in the U.S. and the existing laws in China, Shanghai Financial Consumer Dispute Resolution Mechanism can be divided into following interrelated aspects:

1. Establish and improve the complaint resolving system to enable the banks, and other financial institutions to handle and solve consumer complaints on their own.
2. Establish a complaint resolving system which has various financial regulators in charge of specialized supervision and Shanghai Financial Office in charge of unified coordination in case

that some financial agencies can't resolve consumer complaints.

3. Specify ways adopted by Shanghai Consumer Rights and Interests Protection Association to resolve financial consuming disputes.
4. Establish the procedures of handing or arbitrating financial consuming dispute in detail by the arbitration commission.
5. As for judicial organs, we suggest that the National People's Congress and the Supreme People's Court might support Shanghai to innovate judicial work on finance. The specific suggestion includes: NPC standing committee approve the establishment of financial court, innovate an assess system of financial judge, and expand the jurisdiction of Shanghai local courts on financial cases.

Conclusion

The legal system that Shanghai International Financial Center wants to build up is an organic part of China's legal system. Therefore, the implementation of the above Suggestions will contribute to the consistent reform and innovation of China's macro legal system. Shanghai legislative, executive and the justice department, Shanghai financial business circle, Shanghai legal profession should take the lead in exploring the legal system and make more contribution. Jurists should work hard on the legal theory so as to perfect the law system in China and accelerate social development.

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